

STATE BOARD OF LAND COMMISSIONERS
MAY 14, 2002

Subject

Request by WestRock Associates LLC (WestRock) to lease approximately 2,124 acres of endowment land located in Valley County for development of a ski resort and golf course. 640 acres of the area belongs to the Public School endowment and the remainder belongs to the State Hospital South endowment.

Background

WestRock first applied to lease endowment land near Lake Cascade in January, 1998. The original proposal included a ski area, restaurants, a mountain hamlet, tennis center, equestrian center and golf course on state land, along with 3600± dwelling units and other amenities on adjacent private land.

The current primary use of the land covered by the application is timber production.

Following review and assessment of the proposal the Land Board directed the Department in September, 1999, to publish a Request for Proposals (RFP) on the endowment land covered by the WestRock application. The RFP was advertised for ten weeks with a closing date of February 23, 2000. WestRock submitted the only proposal. In accordance with the terms of the RFP, the Director appointed a seven-person Proposal Review Committee (PRC) to review the proposal and report on its completeness and feasibility.

The RFP process also required a public hearing which was held on April 13, 2000 in McCall. Approximately 350 people attended. Based on sign-up sheets and comments, those in attendance favored the project by about a two to one margin.

In February 2001 WestRock submitted a refined proposal that downsized the project considerably. The downsized project was reviewed by the PRC. The PRC report indicated that the site appeared to meet the needs for the development WestRock proposed in terms of weather and snow conditions, but, "found it impossible to evaluate the request for lease of state land separate from the private real estate development. The ski (area) development must have the capital and income infusion from the real estate development to survive and prosper." The committee requested review of the real estate component of the proposal by "someone knowledgeable."

Discussion

Since receipt of the refined proposal the Department has worked diligently to analyze the financial viability and potential environmental impacts of the project as envisioned. A key issue is whether the potential returns, balanced against the potential risks, is in the best long-term interests of the endowments.

In this process the Department has reviewed the terms, conditions, and financial arrangements at a number of ski areas and four-season resorts throughout Idaho and the United States. We have met with the Valley County Commissioners, and have examined the comments presented

at public meetings on the subject. Our goal has been to provide an objective review of the facts and the merits of the proposal.

During this period WestRock has been working with other state agencies, pertinent federal agencies, and local entities to identify and attempt to resolve issues and concerns.

As a result of these efforts:

- The Valley County Planning and Zoning Commission unanimously approved, on May 8, 2002, the WestRock development plan, and issued the conditional use permits necessary for WestRock to begin development.
- The Department of Environmental Quality and WestRock have finalized a Memorandum of Agreement for water quality monitoring, analysis and review.
- The Department of Transportation and WestRock have been negotiating transportation system improvements indicated by the proposal and are establishing a Memorandum of Agreement for such improvements.
- The Department of Water Resources (IDWR) has received a municipal water right application from WestRock. The application has been protested. An IDWR hearing on the application has been delayed until such time as the Land Board makes a final decision regarding WestRock's lease application. IDWR has approved stream channel alteration permit applications for Rock Creek and Poison Creek.
- The United States Army Corps of Engineers has issued permits required for installing access roads and culverts and to begin wetland mitigation projects.
- The Idaho Department of Parks and Recreation and WestRock have signed a Memorandum of Understanding for mitigation of five public campgrounds that would be affected by the WestRock development.
- The Idaho Department of Fish & Game and WestRock have agreed to a Memorandum of Understanding which provides for riparian and wetland mitigation and water quality and habitat improvements. As a part of the agreement WestRock will donate \$150,000 in matching funds to improve wildlife habitat and water quality improvement in the Lake Cascade drainage.

The Land Board held a hearing in February 2002 to accept additional public testimony and comments on the project. In March 2002, the Board directed the department to work with WestRock to resolve ten specific issues associated with the proposed lease. Those items included the specific lease terms, rental rates, pre-conditions to construction, environmental issues, bonding, mortgage rights, title to improvements, timber removal, water rights, and the actual lease acreage. Based on Board direction, Deputy Attorney General Kent Nelson has taken a lead role in negotiating these issues and drafting the state's lease document.

As a result of these negotiations the Department has developed a lease with terms designed to address the state's concerns, to adequately compensate the endowments for the use of the lands, and to mitigate through bonding against the risks associated with the project.

The Department position in these negotiations was based on five basic considerations:

1. The realized annual rent, after oversight costs and administration, must exceed the current revenue from timber production including a reasonable buffer against additional risks associated with the proposal.
2. Payments to the endowments must be front-end loaded to ensure a reasonable return regardless of the success of the proposal.
3. In order to simplify the calculation and collection of rental, rent should be a fixed rent for at least the first ten years of the lease.
4. If or when rent is based on a percentage of gross receipts, the calculation of gross receipts must reasonably reflect the contribution of the endowment land to the success of the resort.
5. Provide adequate protection against the financial and environmental risks associated with the proposal through lease terms and bonding.

Basic lease terms are outlined on Attachment 1, and include the following:

A. Lease Term

The lease shall be issued for an initial 10-year term, with provision for an automatic extension to 49 years upon legislative approval of long-term leasing of the site.

B. Authorized Uses of the Leased Premises

WestRock is authorized to use of the property for ski hill and related outdoor recreation, and for a portion of the resort's 18-hole golf course. The public can use the land for other purposes which are not incompatible with the resort. The State retains the right to lease the property for uses other than those for which WestRock is paying rent (leasing for these uses will be exclusive to WestRock). The State will not lease the site for a use that is incompatible with the resort uses.

The State retains the right to develop single family or multiple family residential units on a seventy acre "Development Envelope" on the northeasterly portion of the leased premises. WestRock's use of this envelope is subject to the development rights of the State. A joint residential and ski amenity project that would be to the mutual benefit of WestRock and the State might be feasible in the future on this area.

C. Rent

Rent is as follows:

- WestRock will pay a flat rate rental of \$200,000 per year for the initial five years of the lease. \$400,000 of this total will be due upon execution of the lease document. The remaining \$600,000 will be payable upon passage of legislation authorizing long-term leasing of the site.

- WestRock will pay a flat rate rental of \$250,000 per year for years six through ten of the lease.
- In year eleven of the lease the State retains the option to convert to rental rate based on a percentage of gross receipts. The rate begins at 2.5% of gross receipts and expands to as much as 4% of gross receipts beginning in year 16.
- Gross receipts are defined as 85% of ski hill lift tickets and access passes, ski equipment rentals, and ski school revenues, 16.67% of golf greens fees and cart rentals, and 100% of revenue derived from other facilities located on state land.
- WestRock retains the right to buy out of the lease within the first ten years of the lease term upon payment of the balance of rent due under the first ten years of the lease, or five years of rent at the then existing rate, whichever is greater.

D. Improvements on the Leased Premises

WestRock will be allowed to construct ski hill and golf course Improvements on the Leased Premises once they have acquired all necessary government permits and approvals, and that WestRock has shown sufficient financial assurance that it can complete a minimum operating ski resort (Phase One) on the leased premises and on adjacent private lands. The only activities allowed prior to meeting the pre-conditions is the work required under the terms of the Corps of Engineers 404 permit.

WestRock has five years in which to meet the pre-conditions for construction, and an additional five years from the time the pre-conditions are met in which to complete the Phase One minimum ski hill improvements.

The State retains ownership of the improvements on the state lands in the event the lease is terminated by default. Upon expiration of the term of the lease, WestRock will have the right, if it chooses, to remove the improvements and reclaim the property. The State retains the right to require WestRock to remove the Improvements and reclaim the property.

The State will be granted a license by WestRock to operate the Phase One ski hill amenities on the private lands in the event WestRock defaults under the lease and the State wishes to continue a ski hill operation for the balance of the lease term.

All construction on the leased premises will be bonded in favor of the State for payment and performance.

E. Reclamation Plan

WestRock is required to provide a Reclamation Plan for the property, subject to Department approval, prior to commencing construction. The plan will set out the means for reclaiming the state lands should the need arise. WestRock will be required to maintain a reclamation bond in favor of the State to ensure funds are available for reclamation as established in the lease.

F. Vegetation Management and Erosion Control Plan

WestRock is required to provide a Vegetation Management and Erosion Control Plan (Management Plan), subject to Department approval prior to commencing construction. WestRock's construction and operation of the improvements on the state lands will be in accordance with the Management Plan. The Department and WestRock will meet annually to discuss contemplated construction and operations for the ensuing year and adjust the Management Plan accordingly.

G. Timber

The State retains ownership and control of all timber on the leased premises. Removal of timber for the ski runs and other improvements will be done under the standard Department policies, adapted where appropriate to the needs of the resort, and the provisions of Idaho Code. Proceeds from the sale of timber removed accrue to the State and are not considered a part of WestRock's rent obligations under the lease.

Upon execution of the lease, the Department will change the primary use of the land from timber production to recreational lease purposes. The Department will not harvest timber from the property during the term of the lease other than as is necessary for the Improvements, forest health, fire prevention and public safety.

H. Water Rights and Water Development

No water rights are currently associated with the state land. WestRock is seeking approval for water rights to be used for resort operations. A portion of the water from these rights will be used on the state land as part of the resort operations, human consumption, irrigation and snow making. In the event the lease is terminated because of a default, the water right associated with the water used on the state lands will transfer to the State. Upon expiration of the lease term, the water right will be treated in the same fashion as leasehold Improvements.

I. Allocation of Risk

The lease calls for standard insurance terms insuring the State's liability for damage or injury arising out of the use and occupation of state land by WestRock. These include requirements that the State be named as an additional insured under the premises liability policy. Additional policies covering construction activities on the state land are also required.

WestRock will maintain casualty insurance coverage of the sort and amount expected of this sort of a business, to ensure that funds are available to reconstruct the resort, including the Improvements on the state lands, in the event of casualty damage.

The lease addresses potential environmental problems associated with the development on a multi-tiered level:

1. WestRock is required to maintain insurance listing the State as an additional insured against liability arising from the release of any hazardous substances brought onto the leased premises by WestRock. The lease limits hazardous substances to those that are reasonably necessary for WestRock's operations on the state lands.

2. Construction of improvements and alteration of the state lands will be governed by Vegetation Management and Erosion Control Plan approved by the Department. This plan will include application of Best Management Practices (BMP) in any construction. Construction contracts will be bonded for performance in accordance with those terms.
3. WestRock and the Idaho Department of Environmental Quality have entered into an agreement calling for an immediate and long-term program of monitoring to detect any increase in runoff or in sediment or phosphate loading from the state lands. The above mentioned Vegetation Management and Erosion Control Plan will incorporate the elements of this agreement.
4. The State retains the authority and obligation to require compliance by WestRock with any applicable state or federal law, including all environmental laws. This authority is independent of and in addition to any jurisdiction the federal or state environmental agencies have to enforce these laws.

J. Single Leasehold Estate - Assignment/Subletting/Mortgages

The lease retains a single leasehold estate through out its term, unless the Board elects otherwise. Assignment can be made only with approval of the Board and approval can be withheld for the purpose of maintaining a single lessee for the entire state land parcel. Any subletting requires Department approval and subleases will be subject to the overall state lease.

The lease allows for mortgaging the leasehold estate by WestRock. Mortgage holders are granted certain rights to cure Lessee defaults and to acquire the leasehold estate through foreclosure if the Lessee does not pay its obligations. In the event a Mortgage holder finds it necessary to take leasehold interest through a foreclosure, the Mortgagee must find an approved Lessee/Operator for the State lands. Approval of any new Lessee/Operator of the state lands is through the Board under a specific time frame.

K. General Terms

The lease contains a full complement of standard Department leasing terms for commercial leases.

Attachment 2 is a draft of the full text of the lease.

We believe the above lease terms and considerations provide for appropriate compensation while protecting the endowments against the financial and environmental risks associated with a project of this magnitude. We believe the package as presented is beneficial to the endowments.

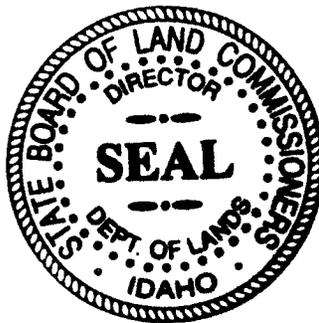
Recommendation

That the Board direct the Department to:

1. Forward the draft lease to WestRock for full execution by signature, provision for bonding, and tendering of the required initial lease payments.
2. Upon full lease execution, reclassify the lands included in the lease from timber production to recreational use as the primary use.

Board Action

A motion was made by Attorney General Lance to adopt the recommendations of the department. Secretary of State Cenarrusa seconded the motion. The motion carried on a vote of 4-1, with Governor Kempthorne, Attorney General Lance, Secretary of State Cenarrusa and Superintendent Howard voting aye; Controller J. D. Williams voted nay.



Attachments

1. Basic lease terms
2. Draft of the full text of the lease